**A PRESENTATION PREPARED FOR ARITA**

# 13 SEPTEMBER 2017

# *Bankruptcy & Self-Managed Superannuation Funds*

Suite 1006, Level 10, 185 Elizabeth Street, SYDNEY NSW 2000
&
Suite 407, Level 4, 49 Queens Road, FIVE DOCK NSW 2046
Ph: (02) 9713 7482
Email: lawyers@danielafazio.com

## ABOUT THE AUTHOR

Daniela founded Daniela Fazio Lawyers Pty Ltd in July 2015, a boutique law firm specialising in insolvency, debt recovery, conveyancing, wills, estates and probate matters, following 10 years working with Sally Nash & Co Lawyers (now known as O'Neill Partners Commercial Lawyers incorporating Sally Nash & Co Lawyers).

Daniela is a Solicitor admitted to practice in New South Wales as well as a Nationally Accredited Mediator.

Holding significant experience acting for Trustees in Bankruptcy, Trustees for Sale, Liquidators, Court appointed Receivers, secured creditors, bankrupts and debtors, Daniela offers proven success supporting corporate clients as well as lay clients to bring finality to all matters efficiently and expeditiously as possible.

## 1. STATISTICS

1.1 According to the Australian Prudential Regulation Authority ("APRA")[1] quarterly statistics, out of the 570,655 superannuation entities in June 2016, 568,315 of those entities were Self-Managed Superannuation Funds ("SMSF").

1.2 Since June 2016, there has been an increase of approximately 5% per year of the number of SMSF as at June 2017 where the number of SMSF sits at 596,516.

1.3 According to AFSA's statistics[2], whilst the number of personal insolvencies have increased by 2.1% in 2016–17, bankruptcies in fact decreased by 5.1% and have fallen every year since 2009 -10 (except for 2015-16).

1.4 Notwithstanding the fact that there has been a decrease in bankruptcies over the last 7 years, it is true to say that bankruptcy numbers are still reasonably high, particular in New South Wales and Queensland. Further, it is evident from the APRA statistics that there are now more SMSF than are tied up in the larger industry funds. Those two factors combined display the importance for a Trustee in Bankruptcy to gain an understanding of the interaction of bankruptcy and SMSF.

## 2. WHAT ARE THE DIFFERENT TYPES OF SUPERFUNDS AND WHO REGULATES THEM?

2.1 There are 3 categories of superfunds. They are:-

(a) APRA regulated, including:-

- Corporate
- Industry
- Public Sector
- Retail
- Single –member Approved Deposit Funds
- Small APRA funds

(b) Deputy Commissioner of Taxation ("ATO") regulated:-

- SMSF

(c) Unregulated superannuation fund.

[1] APRA Statistics – Quarterly Superannuation Performance June 2017 (issued 22 August 2017)

[2] AFSA Statistics – Provisional annual personal insolvency statistics 2016-17

## 3. VESTED PROPERTY v NON DIVISIBLE PROPERTY

3.1 General rule as to vesting of property upon bankruptcy is set out at s58(1) of the Bankruptcy Act.

3.2 Whilst s116(1) of the Bankruptcy Act provides for circumstances in which property (as defined in s5 of the Bankruptcy Act or vested bankruptcy property as defined in s4 of the Family Law Act, 1975 (Cth)) vests in the Trustee in Bankruptcy for the benefit of the unsecured creditors in the bankrupt estate, s116(2) of the Bankruptcy Act sets out the circumstances where property will not be divisible amongst the unsecured creditors of the bankrupt estate.

3.3. Relevantly, for the purpose of this paper, s116(2)(d) of the Bankruptcy Act provides:-

> *"(2) Subsection (1) does not extend to the following property:*
> *(d) subject to sections 128B, 128C and 139ZU:…*
> *(iii) the interest of the bankrupt in:*
> *(A) **a regulated superannuation fund** (within the meaning of the Superannuation Industry (Supervision) Act 1993 ); or*
> *(B) an approved deposit fund (within the meaning of that Act); or*
> *(C) an exempt public sector superannuation scheme (within the meaning of that Act);*
> *(iv) a payment to the bankrupt from such a fund received on or after the date of the bankruptcy, if the payment is not a **pension** within the meaning of the Superannuation Industry (Supervision) Act 1993…";*

3.4 Note that a payment of the type referred to in s116(2)(d)(iv) of the Bankruptcy Act does not stipulate that the payment must be made to the bankrupt from his or her super fund and therefore it can come from a third person's regulated super fund (such as a mother, a sibling, a wife, or an unrelated party).

## 4. Unregulated superfund v Regulated

4.1 The interest of a bankrupt in a regulated superannuation fund within the meaning of the Superannuation Industry (Supervision) Act, 1993 ("SIS Act") is non divisible property. Therefore the starting point should, in my view, be to consider the definition of "*a regulated superannuation fund"* in the SIS Act.

4.2 A regulated superannuation fund is defined in s19 of the SIS Act. A superannuation fund will be a regulated superannuation fund if it complies with s19(2) to (4) of the SIS Act which requires in summary:-

> "*(1) A regulated superannuation fund is a superannuation fund in respect of which subsections (2) to (4) have been complied with. Fund must have a trustee*
>
> *(2) The superannuation fund must have a trustee.*

*Trustee must be a constitutional corporation or fund must be a pension fund*

*(3) Either of the following must apply:*
*(a) the trustee of the fund must be a constitutional corporation pursuant to a requirement contained in the governing rules;*
*(b) the governing rules must provide that the sole or primary purpose of the fund is the provision of old-age pensions.*

*Election by trustee*

*(4) The trustee or trustees must have given to APRA, or such other body or person as is specified in the regulations, a written notice that is:*
*(a) in the approved form; and*
*(b) signed by the trustee or each trustee;*
*electing that this Act is to apply in relation to the fund…"*

4.3 There is a mandatory requirement for certain funds to be regulated. Those requirements are contained in s19(7) of the SIS Act:-

*"(7) If all of the following conditions are satisfied in relation to a superannuation fund at any time during the period beginning on the day on which this Act received the Royal Assent and ending at the end of the fund's 1993-94 year of income:*
*(a) the fund has a trustee;*
*(b) either:*
*(i) the trustee of the fund is a constitutional corporation; or*
*(ii) the governing rules of the fund provide that the sole or primary purpose of the fund is the provision of old-age pensions;*
*(c) the fund is not a public sector superannuation scheme;*
*(d) there is in force a notice under section 12 or 13 of the Occupational Superannuation Standards Act 1987 stating that the Commissioner is satisfied that the fund satisfied, or should be treated as if it had satisfied, the superannuation fund conditions in relation to a particular year of income;*
*(e) there is not in force a notice under section 12 or 13 of the Occupational Superannuation Standards Act 1987 stating that the Commissioner is not satisfied that the fund satisfied the superannuation fund conditions in relation to a year of income later than the year of income mentioned in paragraph (d);*

*the trustee of the fund* ***must use its best endeavours*** *to ensure that the fund becomes a regulated superannuation fund at or before the beginning of the fund's 1994-95 year of income."*

4.4 Although there is a mandatory requirement for certain funds to be regulated (and this appears to include a SMSF), a contravention of s19(7) of the SIS Act is not an offence per se but it is a ground for an injunction under s315 of the SIS Act.

4.5 So what is the Trustee of a regulated superannuation fund responsible for? They are responsible for ensuring that the core purpose of the superannuation

fund is to provide benefits to members of the fund on their retirement, the attainment of a prescribed age or, on their death, to the members' legal personal representatives and/ or dependents.

4.6 The "core purpose" of a regulated fund is defined in s62(1)(a) of the SIS Act. Each Trustee of a regulated super fund must ensure the fund is maintained solely for the provision of benefits for each member for one or more of the following purposes:-

- On or after the members retirement.
- On or after the members attainment of the "retirement age" not less than as required by the Regulations.
- The earlier of the member's retirement or the member attaining "retirement age."
- Upon death and the benefits to be provided to the members legal personal representative, to any or all of the members dependents or to both.

4.7 Note that there are ancillary purposes of a regulated fund defined in s62(1)(b) of the SIS Act.

4.8 It should be noted here that an unregulated and/or a non-complying superannuation fund can become a regulated and complying superannuation fund if it passes the test in s42A(5) of the SIS Act.

4.9 What does s42A of the SIS Act say? It says in a nutshell:-

*"the entity (meaning the superfund) was a resident regulated superannuation fund at all times during the year of income when the entity was in existence or other than a time before it became a resident regulated superannuation fund and it passes the test in subsection 5.*

*an entity passes the test in this subsection in relation to a year of income or part of a year of income if* ***no trustee of the entity contravened any of the regulatory provisions*** *in relation to the entity during the year of income or part of the year of income or if the trustee did contravene one or more of the regulatory provisions, the regulator has determined that, despite the non - compliance, it "thinks" that a notice should nevertheless be given stating that the entity is a complying superannuation fund in relation to the year of income concerned."*

4.10 In determining that notwithstanding there is a non-compliance with the SIS Act the Regulator has the power to deem that entity as complying, by taking into consideration factors such as:-

- The tax consequences that are likely to arise if the entity were to be treated as a non-complying superannuation fund (noting a non-complying superfund is taxed at 45%).

- The seriousness of the contravention or the contraventions; and

- Any other relevant circumstances.

4.11 Consider the decision of Smith J in the matter of *Jones v Official Receiver & Anor* [2017] FCA 1101 delivered on 9 May 2017.

4.12 In considering whether the "My Prerogative Superannuation Fund" was a "regulated superannuation fund" for the purposes of s128B of the Bankruptcy Act, at paragraph [60] His Honour in the *Jones* decision said:-

*"First and most simply, Mr Jones (the bankrupt) said that it was [a regulated superfund] in his statement of affairs. Secondly by letter dated 1 March 2013 addressed to the fund's trustee, the Deputy Commissioner of Taxation confirmed that the fund was a "complying superannuation fund" is a "resident regulated superannuation fund" that complies with certain requirements of s42 of the SIS Act [as opposed to s42A SIS Act].*

4.13 Whilst a superannuation fund is not in a regulated fund, approved deposit fund or an exemption public sector scheme, the fund does not gain the protection of s116(2)(iii)(A) of the Bankruptcy Act, 1966 (Cth) ("Bankruptcy Act").

## 5. IS THE BANKRUPT'S ASSERTED SELF-MANAGED SUPERANNUATION FUND REALLY A SELF- MANAGED SUPERANNUATION FUND?

5.1 After determining whether the fund is a regulated fund the next consideration must be to determine whether that regulated fund is a SMSF as defined by the SIS Act (and you may be satisfied that the Regulator's notice is sufficient evidence that the fund is regulated).

5.2 Section 17A of the SIS Act defines the phrase "*self – managed superannuation fund"* to mean:-

***"Definition of self managed superannuation fund***

*Basic conditions--funds <u>other than single member funds</u>*

*(1) Subject to this section, a superannuation fund, other than a fund with only one member, is a **self managed superannuation fund <u>if and only if</u>** it satisfies the following conditions:*

*(a) it has fewer than 5 members;*

*(b) if the trustees of the fund are individuals--each individual trustee of the fund is a member of the fund;*

*(c) if the trustee of the fund is a body corporate--each director of the body corporate is a member of the fund;*

*(d) each member of the fund:*

*(i) is a trustee of the fund; or*

*(ii) if the trustee of the fund is a body corporate--is a director of the body corporate;*

*(e) no member of the fund is an employee of another member of the fund, unless the members concerned are relatives;*

*(f) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;*

*(g) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any duties or services performed by the director in relation to the fund.*

*Note: Section 17B contains exceptions to paragraphs (1)(f) and (g).*

*(2) Subject to this section, a superannuation fund with only one member is a **self managed superannuation fund** if and only if:*

*(a) if the trustee of the fund is a body corporate:*

*(i) the member is the sole director of the body corporate; or*

*(ii) the member is one of only 2 directors of the body corporate, and the member and the other director are relatives; or*

*(iii) the member is one of only 2 directors of the body corporate, and the member is not an employee of the other director; and*

*(b) if the trustees of the fund are individuals:*

*(i) the member is one of only 2 trustees, of whom one is the member and the other is a relative of the member; or*

*(ii) the member is one of only 2 trustees, and the member is not an employee of the other trustee; and*

*(c) no trustee of the fund receives any remuneration from the fund or from any person for any duties or services performed by the trustee in relation to the fund;*

*(d) if the trustee of the fund is a body corporate--no director of the body corporate receives any remuneration from the fund or from any person (including the body corporate) for any duties or services performed by the director in relation to the fund.*

*Note: Section 17B contains exceptions to paragraphs (2)(c) and (d).*

5.3 There are exceptions to the definition of a self-managed superfund. The exceptions appear in s17B of the SIS Act and allow for the Trustee of the SMSF (whether personal or corporate) to be remunerated if the Trustee performs his/her/its services for the SMSF:-

- other than in his/her/ the Directors capacity as Trustee of the SMSF
- is appropriately qualified to perform the duties or services and holds all necessary licences to perform those duties or services
- Duties or services performed in the ordinary course of business
- The remuneration is no more favourable to the Trustee than that which is reasonable.

5.4 Also consider Regulation 1.04aa of the Superannuation Industry (Supervision) Regulations, 1994 (Self-Managed Superannuation Funds--Persons Not Taken To Be Employees.

5.5 A bankrupt is disqualified from being a Trustee of a SMSF. Each member of the fund must be a Trustee and each Trustee must be a member of the fund (except for single member funds which requires 2 Trustees and 1 of those Trustees must be a fund member). Consider whether then, as a regulated superfund the superfund a trustee is now a bankrupt can pass the test set out in s42A(5) of the SIS Act or how is he/she to meet the requirements of s17A of the SIS Act? What happens now if that superfund cannot pass the test?...Hold your thoughts – there are more factors to consider.

5.6 Anyone over the age of 18 years of age can be a Trustee of a superfund (or a Director) as long as they are not under a legal disability or a disqualified person (includes an undischarged bankrupt); s201B(1) of the Corporations Act, 2001.

5.7 A bankrupt cannot be a Director of a company and therefore cannot be a Director of a corporate Trustee of a SMSF. Each member of the fund must be a Director of the company and each Director of the corporate Trustee must be a member of the fund (except in the case of a single member fund where the Trustee company may have 1-2 Directors but no more. The fund member must be either the sole Director or 1 of 2 Directors.

## 6. OBLIGATIONS OF A SELF- MANAGED SUPERFUND

6.1 Part 4 Division 3 of the SIS Act outlines the obligations for self -managed superannuation funds.

6.2 s35AE SIS Act:

*"**Accounting records***
*Accounting records must be kept etc.*
*(1) Each trustee of a superannuation entity that is a self managed superannuation fund must ensure that:*
*(a) accounting records that correctly record and explain the transactions and financial position of the entity are kept; and*
*(b) the accounting records of the entity are kept in a way that enables the following to be prepared:*
*(i) the accounts and statements of the entity referred to in section 35B;*
*(ii) the returns of the entity referred to in section 35D; and*
*(c) the accounting records of the entity are kept in a way that enables those accounts, statements and returns to be conveniently and properly audited in accordance with this Act…"*

6.3 Each Trustee of the superannuation entity must also ensure that:[3]

[3] S35AE((2) Superannuation Industry (Supervision) Act, 1993

- The records are kept for at least 5 years after the end of the year of income to which the transactions relate; and

- The records are kept in Australia; and

- The records are kept in writing in the English language or in a form in which they can be readily translated.

6.4 s35B SIS Act:-

> *"**Accounts and statements***
>
> (1) *Each trustee of a superannuation entity that is a self managed superannuation fund must, in respect of each year of income of the fund, ensure that the following accounts and statements are prepared* in respect of the entity:
>
> (a) except where the regulations provide that this paragraph does not apply--a statement of financial position;
>
> (b) except where the regulations provide that this paragraph does not apply--an operating statement;
>
> (c) the accounts and statements specified in the regulations.

6.5 Also consider Part 8 of the Superannuation Industry (Supervision) Regulations, 1994- Financial Reporting requirements:-

Reg 8.01 Accounts--statement of financial position and financial statement
Reg 8.02 Accounts and statements that must be prepared
Reg 8.02A Period within which an auditor must be appointed
Reg 8.02B Asset must be valued at market value
Reg 8.03 Period within which audit report must be given

6.6 s35C SIS Act:-

> **"*Audit of accounts and statements***
> *(1) For each year of income, each trustee of a superannuation entity that is a self managed superannuation fund must ensure that an approved SMSF auditor is appointed to give the trustee or trustees a report, in the approved form, of the operations of the entity for that year. The appointment must be made within whichever of the periods set out in the regulations applies to the entity…"*

## 7. THE CASES

7.1 **Case Study: *Coshott v Coshott* [2013] FCA 907 (10 September 2013)** ("the primary Coshott decision").

The principal issue and on the appeal was whether the bankrupt's interest in the property was held on trust for the Coshott Family Superannuation Fund and therefore not divisible among his creditors. Both the primary Judge and the Full Court of the Federal Court determined that the property was not held on trust for the Coshott Family Superannuation Fund by the bankrupt and that the whole of the bankrupt's interest in the property was held by him beneficially and thus vested in his Trustee in Bankruptcy.

Facts:

- On 9 July 1998 a company known as Schlotzsky's Nominee Pty Ltd ("Schlotzsky") is registered where the purported Directors since inception and to at least 10 September 2013 were Mr Robert Coshott ("Robert") and his wife Ljiljana Coshott ("Ljiljana").

- Ljiljana was and remained as at the date of the primary Coshott decision the sole shareholder.

- On 22 September 2000 a Deed of Trust for the SMSF is executed by the members of the fund under seal of the nominated corporate Trustee, Schlotzsky.

- The members of the fund were Robert, Ljiljana and their sons James and Michael notwithstanding the fact that at the time the Deed of Trust was executed, both James and Michael were under the age of 18.

- On 5 October 2000, Mr Senan Meaney, then a partner of Trood Pratt and Co, Chartered Accountants, signed a certificate stating that the superannuation fund complied with the relevant superannuation laws and that the superfund had elected to become "regulated" and had been issued with an ABN.

- By letter dated 6 November 2000, the Australian Taxation Office ("ATO") advised that the superfund had now been issued with a tax file number and the ATO confirmed that the notice of election to become a regulated superannuation fund was received on 3 October 2000 and that the fund was "now a regulated superannuation fund".

- At trial, the principal of Trood Pratt & Co, Mr Trood gave evidence that he had no knowledge of the establish of the super fund and in fact, he had no record of Trood Pratt & Co ever having acted in any capacity for the fund or the Trustee, including as tax agent or auditer of the Trust.

- Robert and Schlotzsky did not identify at trial or produce any accounts, financial statements, statements of members' interests, statements of assets and liabilities, income tax returns or any other record of any kind

in relation to the superfund which inevitably led the Court to to the inference that no such documents exist or had ever existed.

- The Court reached the conclusion that the fund remained inactive from the time of its establishment or, if there was any activity at all, no record was ever made of it.

- The only things that were ever claimed in the proceedings as activity on behalf of the superfund were transactions reflected in statements from a Bank account operated by Schlotzky, nominally as trustee for the superannuation fund and cancelled cheques from that account.

- At [5] of the primary Judge's reasons he found:-

  *"Schlotzsky's activities, which were almost wholly unexplained, were clearly not confined, despite the name of its business cheque account, to acting as trustee for the superannuation fund. Indeed there is no evidence that anything done by or in the name of Schlotzsky relation to the superannuation fund in any way."*

- Robert's initial claim was that he purchased his 50% interest in the subject property as trustee for the Coshott Family superfund. The premise upon which that claim depended was that, at some time prior to 3 June 2003, he became the trustee (or a trustee) of the superfund in substitution for Schlotzky.

- Robert's alternate argument was that he held his 50% interest in the property pursuant to a resulting trust in favour of Schlotzky. The problem with argument is that Robert would then appear to be accepting that Schlotzky is (and was at all relevant times) the corporate trustee of the superannuation fund and that Mr Coshott is not (and was not) the Trustee.

- Roberts 2 arguments contradicted each other because they postulate different Trustees of the superannuation fund at the time the property was purchased.

- The property was the matrimonial home of Robert and Ljiljana. They lived in the house with their 2 sons, James and Michael.

- The bankruptcy Trustee formed the view that the 50% interest held by Robert in the property, was an asset to be brought to account in his bankrupt estate.

- Buchannan J determined that any suggestion or arrangement tending to suggest that the bankrupt purchased the 50% interest in the property

otherwise than beneficially was a sham and a declaration was made that the bankrupt's interest vested in the Trustee in Bankruptcy from the date of bankruptcy and other ancillary orders, including orders for sale.

## 7.2 Case study: *Coshott v Prentice* [2014] FCAFC 88 ("the Appeal")

Facts:

- On appeal Liljana and Schlotzsky's challenged the declarations and orders for sale and argued that the primary Judge gave undue weight to "irrelevant" or "unimportant" considerations relation to the operation of the superannuation fund and its Bank account. Those "irrelevant" or "unimportant" considerations were the fact that the primary Judge considered:-
    - Irregularities in the superannuation fund records and evidence that the fund's bank account was sometimes used for other purposes;
    - The fact that the purchase of the interest in the property was not authorised by the Trust Deed and would have contravened the SIS Act.
    - The consideration that Robert could not have been the Trustee of the Coshott Family Superfund.
    - The fact that the solicitor acting for Robert and Ljiljana on the purchase of the property was instructed to purchase the property for them as joint tenants.
    - The Trust Deed made express reference to the SIS Act and Regulations.
    - The members of the Coshott Family Trust were Robert, Ljiljana, James and Michael.
    - Problem? James and Michael were minors at the time the Coshott Family Trust was created so they could not be Directors of any company. It follows therefore that when the Coshott Family Superannuation Fund was purportedly established, it was not possible for the Trustee, as a constitutional corporation, to comply with the express requirements of either the Trust Deed or the SIS Act that **all** members be Directors of the corporate Trustee of the super fund.

7.3 Some of the challenges/ hurdles which arose for the Coshott family both in the primary Coshott decision and then on appeal was that his argument that he held his interest on trust for the Coshott Superannuation Fund was flawed because of the facts that:-

- The property was purchased as joint tenants and not tenants in common – the effect of the Coshott Family Superannuation Fund owning half an interest in the property with Ljiljana as joint tenants would mean that the interests would blend together pursuant to the rules of survivorship in the event of death of one purchaser.

- A superannuation fund cannot own the home in which its members resided;

- The land tax would be substantially more if a superannuation fund had an interest in the property because the principal place of residence exemption would be lost.

- 2 of the members were minors and therefore could not be Directors. One of the purported Directors was a bankrupt and thus disqualified from being a Director.

- After Robert was made bankrupt, Robert and the other members of his family sought to raise funds on the security of the property to obtain an annulment of his bankruptcy and this included transferring their interest in the property to James and Michael.

**7.4 Case study: *Trustees of the Property of Morris (Bankrupt) v Morris (Bankrupt)* [2016] FCA 846 (22 July 2016)**

Concerns a regulated superfund and not a SMSF but is a good example of what can happen when bankruptcy, death benefits and the payment of those death benefits intermingle.

The Court was asked by the Trustee of the property of Mrs Morris (the bankrupt) to determine whether two payments which she received after the date of bankruptcy from her late husband's estate, were divisible property amongst her creditors or whether the payments were of the type excluded by s116(2) of the Bankruptcy Act.

Facts:

- Mr Foreman and the bankrupt married and had 2 children (both of the children were minors at the time of the hearing).

- Mr Foreman died in May 2013 and the bankrupt was left widowed with 2 minor children.

- Mr Foreman had an interest in 2 Super Funds; AustSafe Super Fund and Plum Superannuation Fund.

- In August 2013, the bankrupt was made bankrupt.

- On December 2013, and at its discretion, the Trustee of the AustSafe Super Fund paid $45,392.48 to the bankrupt.

- On 26 March 2014, and at its discretion the Trustee of the Plum Superannuation Fund paid $67,240.27 to the bankrupt ("Plum super payment").

- The Trustees in Bankruptcy argued that the 2 payments did not fall within any of the items listed in s 116(2) of the Bankruptcy Act and thus were caught by s 116(1) and therefore divisible amongst the bankrupt's creditors.

- Obviously the bankrupt disagreed with the Trustees in Bankruptcy and she argued that, the 2 payments, fell within either or each of the s116(2)(d)(iii)(A) or s 116(2)(d)(iv) of the Bankruptcy Act. Further, or alternatively in respect of the Plum Super payment, the bankrupt argued that the payment, in any event, fell within the definition of s116(2)(a) of the Bankruptcy Act, being property held by the bankrupt in trust for another person (ie, her children). As to the latter argument, there was a dispute between the parties as to whether an inference ought to be drawn as to whether the payment to her from Plum Super was **just** a payment to her, or whether the payment to her was for her benefit and the benefit, education and maintenance of the minor children.

- Mr Foreman did not complete a Binding Death Nomination in either Super fund specifying who the beneficiaries of his superannuation were to be upon death.

- The Court looked to the Trust Deeds of each Super fund. Those Trust Deed each authorized the Trustee of the Superfunds to use their discretion when making payments to its members and their dependents.

- One of the submissions made by the Trustees of the bankrupt estate at the hearing was that it was not Parliaments intention when drafting s116(2)(d) of the Bankruptcy Act to exempt the interest of a bankrupt's spouse or partner or a payment from such a superannuation fund but rather it was only Parliament's intention to exempt the interest of a

bankrupt in a regulated superannuation fund or, for that matter, a payment **from** such a fund.

- The Court held that each of the Super funds had the discretion to pay the proceeds of Mr Foreman's superannuation to the bankrupt and her dependent children. The bankrupt had no interest in either of the funds. The bankrupt and her minor children were nothing more than "objects of a discretionary power." The bankrupt and her minor children had a right to the due administration of each of the Super funds in accordance with the Trust Deeds but no more. As a result, their interest in the proceeds of the Super fund were not proprietary in nature but were at the favourable end of the Trustees exercise of the discretion afforded to each of them, which was an interest in a regulated superannuation fund.

- The Court found that s116(2)(d) of the Bankruptcy Act was not applicable but rather than the bankrupts interest in each instance fell within s116(2)(d)(iii)(A) of the Bankruptcy Act.

7.5 Contrast the *Morris* decision with the most recent decision of *Cunningham (Trustee) v Gapes, in the matter of Gapes (Bankrupt)* [2017] FCA 787 (13 July 2017).

**7.6 Case study: *Cunningham (Trustee) v Gapes, in the matter of Gapes (Bankrupt)* [2017] FCA 787 (13 July 2017).**

In *Cummingham's* case, the payment of the sum of $87,900.33 from the bankrupt's late mothers estate which formed part of her regulated superannuation fund was held to be property divisible amongst the creditors of Mr Gapes bankrupt estate.

Facts:

- On 17 January 2011, the bankrupt was declared bankrupt and John Cunningham was appointed the Trustee of his bankrupt estate.

- On 18 December 2013, the bankrupt's mother died and the bankrupt (an undischarged bankrupt at that time), was named as a joint executor and joint beneficiary in her will.

- On 14 February 2014 a Grant of Probate was obtained in respect of the will. The major asset in the mother's deceased estate was the proceeds of her regulated superannuation fund which had a balance of $248,696.49.

- The Trustees of the super fund subsequently paid those funds **to the solicitors** acting on behalf of the executors of the mother's deceased estate.

- On 12 March 2014 and pursuant to the terms of the mother's will, the executors of the mother's deceased estate distributed $263,700.98 to the beneficiaries including the bankrupt who received $87,900.33.

- The cheque payable to the bankrupt was for $87,900.33 and **received from the executors** of his mother's deceased estate, was **deposited into his wife's Bank account** because according to the bankrupt, he did not have a Bank account at that time.

- When the bankrupt's Trustee became aware of the payment of $87,900.33 to the bankrupt and the fact that the bankrupt deposited the cheque into his wife's Bank account, the Trustee naturally made a demand on the bankrupt's wife for the payment asserting that it was after-acquired property in the bankrupts estate.

- The bankrupts wife declined the Trustee's demand to pay him the $87,900.33 asserting that because the moneys came from a regulated super fund they were protected by the provisions of section 116(2)(d) (iv) of the Bankruptcy Act.

- The Trustee commenced proceedings in the Federal Court seeking declarations & orders that the $87,900.33 was an after-acquired asset and not protected by s116(2)(d) (iv) of the Bankruptcy Act and that the bankrupt's wife pay him the $87,900.33.

- The bankrupt's wife maintained her position that the $87,900.33 was protected because it was a payment to her bankrupt husband from a regulated super fund…but was it??

- The Court found in favour of the Trustee accepting his submissions that:

  (a) Whilst the bankrupt had an interest in his mother's deceased estate, **he did not** have an interest in his mother's super fund, and

  (b) The bankrupt did not receive the subject $87,900.33 direct from his mother's super fund, but rather the payment came from his mother's deceased estate.

  (c) Therefore the payment was not "*a payment received by the bankrupt from a regulated superannuation fund*" and

consequently it was **not** protected by the provisions of s116(2)(d)(iv) of the Bankruptcy Act.

(d) Once the $248,696.49 held in the mother's super fund was paid into the mother's deceased estate, it **lost its character** as super funds.

7.7 Important to note here that ss58 and 116(1) of the Bankruptcy Act are concerned with "property" and not the character of that property.

7.8 Therefore, consider whether the Court would have reached different conclusion in the event the bankrupt's mother either:-

(a) Nominated the bankrupt as a beneficiary of her super in a Binding Death Nomination and the Trustee of her superfund paid the sum of $87,900.33 to the bankrupt and then the bankrupt pays the money to his wife's Bank account; or

(b) In the absence of such Binding Death Nomination, the Trustee of her superfund was entitled to exercise a discretion and pay to the bankrupt the sum of $87,900.33 direct from the mother's superannuation fund but the bankrupt directed the proceeds to be paid to his wife's Bank account; or

(c) Nominated the bankrupt as a beneficiary or the Trustee of the superfund exercising its discretion paid the proceeds direct to the bankrupt.

## 8. WHAT HAPPENS IF THE BANKRUPT'S ASSERTED SELF-MANAGED SUPERFUND IS DEFICIENT IN SOME WAY (NON-COMPLIANCE ISSUES)?

8.1 Short answer – it will depend.

8.2 If the SMSF does not comply with the requirements made essential by the SIS Act and no exceptions apply, it could potentially leave a gap in the SMSF which the Trustee in Bankruptcy can "attack."

8.3. Also consider record keeping and audit requirements under the SIS Act.

8.4 If the ATO issues a Notice stating that the superfund complies with the requirements of the SIS Act but there is a contravention in some way, the Trustee may commence proceedings in the Administrative Appeals Tribunal to set aside the ATO's decision if adverse to the Trustee in Bankruptcy's position BUT consider the practicalities of this.

8.5 The ATO has power under s289 of the SIS Act to make orders where a person has failed to comply with a requirement under the SIS Act:-

*"Powers of Court where non-compliance with this Act*

*(1) This section applies if the Regulator is satisfied that a person has, without reasonable excuse, failed to comply with a requirement made under this Act.*
*(2) The Regulator may by writing certify the failure to the Court.*
*(3) If the Regulator does so, the Court may inquire into the case and may order the person to comply with the requirement as specified in the order."*

8.6 The fact that a Trustee of a SMSF is a disqualified person does not automatically invalidate an appointment or transaction; s127 of the SIS Act. It is not fatal because there is a grace period of 6 months to remedy the non-compliance.

8.7 Note s349A of the SIS Act:-

*"**Payment out of a fund in accordance with the Bankruptcy Act 1966***

*If a member of an approved deposit fund or of a regulated superannuation fund becomes a **bankrupt**, within the meaning of subsection 5(1) of the Bankruptcy Act 1966 , nothing in this Act, the regulations or the prudential standards prevents a trustee of the fund from paying to the trustee in bankruptcy an amount out of the fund that is property divisible amongst the member's creditors, within the meaning of section 116 of the Bankruptcy Act 1966."*

8.8 It is possible for the Trust Deed to be varied by Court order. Two examples of this include the decisions of the Supreme Court of South Australia on 8 August 2016 of *Westpac Securities Administration Ltd v Cooper* [2016] SASC 122 ("Westpac Securities") and *Retail Employees Superannuation Pty Ltd v Pain* [2016] SASC 121 ("Retail Employees").

8.9 In *Westpac Securities* the Trustee of the Westpac Mastertrust Fund sought to vary the terms of the fund's Trust Deed to give the Trustee power to effect a successor fund transfer without the members' consent. The Court granted the Trustee's application finding that the variation was ultimately in the interests of its members.

8.10 In *Retail Employees* the Trustee of the Retail Employees Superannuation Trust sought an order from the Court varying the Fund's Trust Deed to validate certain previous amendments with prospective effect, which the Trustee considered may not have been made in full compliance with the Trust Deed's amendment clause. The Court made the order as sought by the Trustee on the basis that it was appropriate to vary the Trust Deed and that the variations were ultimately in the interests of the members.

8.11 Also consider the decisions of the Superannuation Complaints Tribunal.

## 9. WHAT INVESTIGATIONS, IF ANY, SHOULD A TRUSTEE UNDERTAKE WHEN DETERMINING WHETHER A BANKRUPT'S ASSERTED SELF-MANAGED SUPERFND IS REALLY A SELF-MANAGED SUPERFUND OR WHETHER IT IS A COMPLIANT SUPERANNUATION FUND?

9.1 Using your powers afforded to you as Trustee in Bankruptcy pursuant to s19AA and, 77 of the Bankruptcy Act, ask questions of the bankrupt and any other relevant party.

*Examples (but not exhaustive)*

- Does it comply with the SIS Act? Is a letter from the ATO certifying the superfund complies/ does not comply conclusive evidence? Consider factors determining superfund complies, if any.
- What were the circumstances in which the property was purchased and the source of funds that were used to purchase it? (If claim real property held on trust for Superfund).
- Check establishment of the superfund and its subsequent activities.
- Does the SMSF have a TFN?
- Evidence of any land tax Notice of Assessment (if relates to land).
- Does the bankrupt or any of its members reside in the property owned by the SMSF? If so, query breach of the "in house asset rule"
- Have any loans been made to the SMSF members?
- Where are the accounting records and what are they?
- When was the last audit? Evidence of any audits.
- Where is the Trust Deed?
- Statement of members and their respective interests
- Income Tax Returns
- Payments to spouses

## 10. ATTACK – WHAT ARE SOME OF YOUR OPTIONS?

10.1 Consider whether s122 of the Bankruptcy Act is applicable/ relevant.

10.2 Demand under s129 of the Bankruptcy Act.

10.3 Voidable transaction provisions pursuant to s128B and/or 128C of the Bankruptcy Act (mirrors ss120/121 of the Bankruptcy Act but superannuation specific).

10.4 Use the common law? Perhaps if formal requirements under a title system have not been complied with.

10.5 Section 37A of the Conveyancing Act, 1919 (if in NSW).

10.6 Only “intent” needs to be established under s37A of the Conveyancing Act whereas the intention to defeat creditors must be the “main purpose” under s128B and/or 128C of the Bankruptcy Act.

10.7 Don’t forget the Family Law Act, 1975!

10.8 s139ZQ Notice.

10.9 Injunction under s315 of the SIS Act.